

ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author: Florez Analyst: Darrine Distefano Bill Number: SB 672
Related Bills: See Legislative History Telephone: 845-6458 Introduced Date: 2-21-03
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Disaster Loss Deduction/Excess Disaster Loss For Disasters That Occur On or After July 1, 2003

SUMMARY

This bill would allow a disaster loss deduction for any disaster that occurs on or after July 1, 2003.

The Franchise Tax Board does not administer the provisions relating to property tax deferral for a Governor declared disaster within the Revenue & Taxation Code. Therefore, this analysis will not address those provisions.

PURPOSE OF THE BILL

It appears that the purpose of this bill is to provide disaster loss tax benefits for future disasters without having to obtain legislation that lists the specific type of declared disaster.

EFFECTIVE/OPERATIVE DATE

This bill would be effective January 1, 2004, and operative for all disaster losses occurring on or after July 1, 2003.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Under California and federal law, a disaster loss occurs when property is destroyed as a result of a fire, storm, flood, or other natural event in an area proclaimed to be a disaster by the President of the United States or, for state law purposes, by the Governor.

Under federal and state tax law, the taxpayer may elect to claim the loss either in the year the loss occurs or in the year preceding the loss. This election allows the taxpayer to file an amended return immediately for the prior year. For state purposes, this election may be made prior to passage of any state legislation allowing special carryover treatment because California conforms to the federal election.

Board Position:

<input type="checkbox"/> S	<input type="checkbox"/> NA	<input type="checkbox"/> NP
<input type="checkbox"/> SA	<input type="checkbox"/> O	<input type="checkbox"/> NAR
<input type="checkbox"/> N	<input type="checkbox"/> OUA	<input checked="" type="checkbox"/> PENDING

Department Director
Gerald H. Goldberg

Date
4/17/03

Nonbusiness disaster losses not reimbursed by insurance or otherwise are deductible under state and federal tax law to the extent each loss exceeds \$100. Total nonbusiness disaster losses are deductible only to the extent that the total loss amount for the year exceeds 10% of adjusted gross income.

California income tax law identifies specific events as disasters that are then allowed additional special carry forward treatment. That is, 100% of the excess disaster loss may be carried over for up to five taxable years, and if any excess loss remains after the five-year period, 50% of the remaining excess loss may be carried over for up to 10 additional years.

Current law allows the taxpayer to claim the disaster loss in the taxable year of the loss or elect to claim the loss for the preceding taxable year. The loss is claimed by filing an original or amended return by the extended due date for the year of the loss.

THIS BILL

This bill would add any disaster that occurs on or after July 1, 2003, to the current list of specified disasters as declared by the President or Governor in the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL). Special disaster treatment would be allowed for losses sustained as a result of a disaster occurring on or after July 1, 2003. Thus, specific legislation would no longer be necessary declaring that losses related to a specific disaster are eligible for special disaster loss treatment.

IMPLEMENTATION CONSIDERATIONS

Current state law connects the term "disaster" to a designated Presidential or Governor declared disaster. This bill does not contain such a connection. Since there are many types of losses a taxpayer can claim, the author may wish to define "disaster" as a Presidential or Governor declared disaster area. This would allow a disaster to be reviewed by a third party (i.e. the President or the Governor) in order to determine what qualifies for disaster loss treatment. The absence of definitions to clarify these terms could lead to disputes with taxpayers and would complicate the administration of the disaster loss treatments.

LEGISLATIVE HISTORY

AB 1X (Cardoza, Stats. 1997, Ch. X3) covered losses for the storms and floods of 1996-97. AB 2456 (Sweeney, Stats. 1998, Ch. 749) covered losses for the storms and floods of February 1998. AB 114 (Florez, Stats. 1999, Ch. 165) covered losses for the winter freeze of 1998-99. AB 44 (Wiggins, Stat. 2001, Ch. 618) covered losses for the earthquake that occurred September 2000 in Napa, California.

OTHER STATES' INFORMATION

Michigan, Minnesota, Massachusetts, and New York conform to the federal provisions that allow taxpayers to claim a disaster loss deduction on their state returns either in the preceding year or in the year of the loss. It appears that legislation, executive order, or proclamation by the President or the Governor is required to identify the area impacted by a disaster that is eligible for federal or state assistance.

Florida does not have a personal income tax. However, monetary relief is provided to citizens and corporations through the Emergency Management, Preparedness, and Assistance Trust Fund. Florida also requires legislation, executive order, or proclamation to identify the area impacted by a disaster.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact for Disaster Losses For Every \$1 Billion in Annual Uninsured Losses (In Millions)			
Fiscal Year Impact	2003-04	2004-05	2005-06
Corporation Tax	-\$1	-\$3	-\$4
Personal Income Tax	-\$4	-\$12	-\$13
Net Impact of bill	-\$5	-\$15	-\$17

Revenue Discussion

Based on historical experience, annual revenue losses generated would be approximately \$15 million for every \$1 billion in qualifying disaster losses, spread over a few years.

Developing estimates of this sort is highly speculative due to inherent uncertainties, e.g. predicting future disasters, the type and magnitude, the extent of insurance/assistance protection, the income characteristics of victims. Earthquake disasters produce the largest impacts because of their potential scope and the infrequency of insurance protection for victims (although this latter issue may improve over time).

The estimated losses were based on California disasters that occurred from 1989 through 2001, (i.e. Northridge earthquake, San Luis Obispo fire, Southern California flood, Shasta wildfires, Landers earthquake, L.A. riots, Humboldt earthquake, East Bay fire, Santa Barbara fire, Loma Prieta quake, and various fires and floods throughout several counties). It is evident that nearly every year is represented and that fires are the more common disasters. According to historic data regarding losses attributable to disasters, the twelve-year average for uninsured disaster losses is approximately \$1 billion annually. Using historic data for these California disasters, the estimate is based on a twelve-year average for losses and includes offsets for basis adjustments, and adjusted gross income limitations.

ARGUMENTS/POLICY CONCERNS

For losses incurred in taxable years beginning on or after 2004, 100% of a net operating loss (NOL) can be carried forward for 10 years under the general rules for NOLs. However, current law provides, at the election of the individual or business taxpayer, that 100% of the excess disaster loss may be carried over for up to five taxable years, and if any excess loss remains after the five-year period, 50% of the remaining excess loss may be carried over for up to 10 additional years. Thus, even though a 15-year carryover period would be allowed, the taxpayer would not be entitled to 100% of the NOL, as is available under the general NOL rules. Not modifying the amount eligible for carryover to 100% for 2004 and later years may be considered inequitable to taxpayers with disaster losses.

LEGISLATIVE STAFF CONTACT

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